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November 17, 1954

Messrs. Sidley, Austin, Burgess & Smith
11 South La Salle Street
Chicago 3, Illinois

Attention: Ray Garrett, Esq.

In re: Rubber Producing Facilities Disposal Commission

Dear Mr. Garrett:

I have your letter of the 5th enclosing, and requesting comment regarding preliminary drafts of, proposed deed, note and mortgage for use on the anticipated government sales of rubber plants in this area. Needless to say, these are comprehensive and well prepared. The following comments are intended as preliminary--and many of them are obviously as to relatively minor matters and some relate particularly to California and will probably not be applicable elsewhere

I assume you have available the California Civil Code (CC) and Code of Civil Procedure (CCP), and also the Pacific Reporter, so that reference thereto without extensive quotation will suffice.

AS TO THE MORTGAGE

1. Preliminarily I assume you know that:

(a) under CCP 580b there can be no deficiency judgment on foreclosure of a purchase money mortgage as to real property. While that statute does not apply to chattel mortgages, in the absence of appropriate segregation that distinction would not appear to make much practical difference; and

(b) in case of maturity acceleration for default in any particular installment or obligation the mortgagor

can reinstate the original terms on curing the particular default and paying costs. (CC 2924c)

2. As to joinder of the chattel and real property mortgages in a single instrument:

Subject to compliance with statutory requirements as to form and recordation of chattel mortgages (as mentioned in later comment as to the mortgage preamble) there appears to be no basic objection to such joinder and it has been recognized as permissible in California,

10 Cal. Jur. 2d, 321

San Francisco Breweries, v. Schurtz, 38 P. 92

Tregear v. Etiwanda Water Co., 18 P. 658

--although in the latter case (on which the San Francisco Breweries case is based) it does not appear there was a sufficient chattel mortgage recording in which event the holding there is only to the effect that such joinder is not per se invalid and that the mortgage was valid as between the parties. The practice of such joinder is not uncommon. It has obvious advantages both in convenience and perhaps in avoiding questions as to whether particular items are personalty or so affixed as to constitute part of the realty. On the other hand, it could conceivably have some small disadvantage in foreclosing if it were desired to foreclose other than by court action. So, real estate mortgages may be foreclosed:

(a) by court action under CCP 726--in which case a year's period of redemption is

allowed; or

(b) by sale under CC2924--if a power of sale is contained in the mortgage, and in such event after three months' preliminary notice, etc., in like manner as in case of foreclosure of trust deeds. Sale in such manner does not allow redemption.

Chattel mortgages, on the other hand, are foreclosed (CC2967):

(a) by action in like manner as real estate mortgages; or

(b) by sale in like manner as prescribed for pledges (CC 3000 et seq.).

Obviously, if sale without court foreclosure action were to be made, a longer period of notice would be required as to the real property than as to the chattel mortgage--although it would appear desirable to sell both at the same time so that should not make any difference. There would not be that differ ence in case of court foreclosure--in which event, however, there would be a redemption period as to the real property, but not as to the chattel mortgaged personal property.

3. Title and preamble of mortgage:

(a) CC 2956 and 2957 require that:

> "A mortgage of personal property * * * shall be clearly entitled on the face thereof, apart from and preceding all other terms of the mortgage, to be a mortgage of crops and chattels, or either, * * *.

On that account I would suggest omitting the word "Purchase" from

the title and recasting the title and first following sentence to read thus:

"Mortgage of Chattels
and also
Mortgage of Real Property

THIS PURCHASE MONEY MORTGAGE OF CHATTELS AND OF REAL PROPERTY, * * *."

(b) I would suggest altering the last four lines on the first page to read:

"America (hereinafter called the Facility), located in the County of _____, in the State of California, and hereinafter more particularly described:

WHEREAS, as part of the consideration therefor the Mortgagor has executed and delivered to said Commission a * * *."

(Note that the latter change would omit the statement that the note is in part payment.)

(c) The form contemplates insertion of a copy of the promissory note. While that is not necessary, I think that in this situation it is better and without it certain statements as to the secured obligation must be made. (CC 2956)

4. Following the description of the property (referred to on page 2 of the draft as "(Copy Groups A, B, C, * * * etc.)), I would insert a rental assignment provision such as is mentioned in later comment as to numbered section 19 of the form.

5. After-acquired property. A chattel mortgage on after-acquired property is valid.

Bank of California v. McCoy, 72 P.2d 923

The present comment relates particularly to the description of such property. With respect to chattel mortgages generally it is, of

course, required that there be a sufficient description of the property--as to which it is said, 10 Cal. Jr. 2d, page 297:

> "Location of the chattels mortgaged is one of the most important elements in the description. Other details without this element often amount to little or nothing, whereas its presence with other slight details may make easy the ascertainment of the property and may make sufficient a description that otherwise would be insufficient. Thus, a description of the chattels as 'all the furniture, upholstery, carpets, draperies, chinaware and other household goods of every kind,' contained in a specified building definitely located and described, is sufficient to identify them, especially where no rights of third parties are involved. Similarly, where mortgaged personal property, consisting of numerous articles which might be found upon any farm, is definitely described as to some items and only generally by name as to others, but all are described as located upon certain described real property which was owned by the defendant at the time the mortgage was given, the description is sufficient in a foreclosure proceeding between the parties."

(Note the reference to validity as between the parties--indicating the necessity for a good description, particularly as to third parties.)

In 10 Cal. Jur. 2d at page 299 it is said:

> "With respect to after-acquired property, the general rule in other jurisdictions seems to be that a mortgage which purports to cover all such property, without any restriction as to its amount, character, or the uses and purposes for which, or the time within which, it is to be acquired, or as to the locality where it is to be placed, is void for indefiniteness. The requirements for sufficiency of description of this class of property have not been directly passed upon in this state, since no question was raised on that point by the cases declaring that after-acquired property is mortgageable irrespective of any doctrine of potential possession."

On that basis I suggest you consider whether the provision regarding after-acquired property (page 2 following the property description)

might perhaps read:

> "together with all fixtures and personal property hereafter acquired by the Mortgagor and placed or located on said mortgaged real property in renewal * * *" etc.

6. Matters as to which the mortgage is made subject.

I understand the purpose of the items listed as (1) to (4) inclusive on pages 2 and 3; but I have had a little difficulty in determining the reason and expedience of the items listed under (5 on page 3, et seq.--particularly subdivisions (a) and (b). It may be there is a practical reason therefor of which I am not aware, based either on existing conditions or anticipated operating neces- sities--in which case the further comment in that behalf may be beside the point. (Incidentally, at the beginning of (a) I note a reference to "nondelinquent liens for taxes", etc. While the obvi meaning is the same, if this feature is to be included it occurs t me it might better read "lien for nondelinquent taxes" since it is the tax, strictly speaking, rather than the lien which may become delinquent).

Many of the matters referred to in (5)--particularly (a) and (b) on page 3, et seq. appear to involve possible claims or liens either existing or which may arise against the mortgagor; and it would ordinarily be expected that a purchase money obligation woul not be subject thereto. In fact, CC 2898 provides:

> "A mortgage or deed of trust given for the price of real property, at the time of its convey- ance, has priority over all other liens created against the purchaser, subject to the operation of the recording laws."

Notwithstanding that section, I have frequently taken the precauti of drawing escrow instructions in form to emphasize and insure tha

no then existing liens against a purchaser, such for instance as judgment liens, should have priority over a purchase money encumbrance. On its face the listing of such items in section 5 would apparently subordinate the mortgage to them, which would appear highly unsatisfactory--particularly in view of the rule that the holder of such a purchase money real estate mortgage must rely solely on it and cannot recover a deficiency judgment.

It is realized that the deed to the purchaser will in effect be a quitclaim necessarily subject to various matters as to which the mortgage must therefore be likewise subject--and some of the items listed under (5) are apparently of that character. However, those items could be covered and the possible subordination to other matters avoided by substituting in lieu of the entire section (5) something such as:

> "Any other liens, charges, or matters subject to which said property was conveyed to mortgagor by said deed."

7. Section 4.

This indicates familiarity with the statutory recording requirements. (CC 2957) The statute does not specify a time for recordation.

> "But the law requires immediate recordation in lieu of immediate delivery in order that a chattel mortgage may be valid as against the creditors of the mortgagor. If a mortgage is withheld beyond a reasonable time, it is void as against creditors of the mortgagor."

10 Cal. Jr. 2d at page 308, citing Wolpert v. Gripton, 2 P2d 767,

> "What may be considered a reasonable time varies with the circumstances." id.

8. Section 5, page 10.

I note the provision for payment "within six months after

the same shall be payable" as to mechanics' liens, etc. Upon proper recordation the mortgage ordinarily has priority over subsequent liens exclusive, of course, of mechanics' liens arising out of work theretofore commenced. So the provision appears unnecessary except as to liens for work commenced at the time of recordation and as to such liens it would seem unnecessary to allow six months for payment in view of the later provision that payment may be withheld pending contest. Unless the circumstances otherwise require, would it not be preferable to provide simply for prompt payment of all such items subject to deferment pending contest and adequate security and so long as in the mortgagees judgment its security is not thereby lessened or impaired.

9. Section 6, page 11.

While this requires the mortgagor to "make all needful and proper repairs thereto and renewals and replacements thereof", it occurs to me that it might be strengthened by specifically requiring reconstruction and replacement of destroyed items. It has bee expressly held that a lessee's covenant to repair does not impose duty to reconstruct or restore damaged premises (Realty v. Rea, 194 P. 1024). For purpose of reference I enclose a copy of the form of trust deed currently in use by Title Insurance and Trust Company, our principal title company; and on the point under discussion I call your attention to the provision of section 1 of tha form.

10. Section 7, page 12.

This provides for payment of taxes "on or before the last da on which the same shall be due and payable". I imagine this was probably intended to allow to and including the last day before delinquency for payment; but in that case it is inconsistent with

insurance company would probably want to pay jointly to the mortgagee and mortgagor in the absence of different authorization from them. It seems to me that if possible it would be preferable to have the insurance written to cover both interests but with full loss payable to the mortgagee and with the separate provision in the mortgage for agreed relinquishment to the mortgagor for repairs, etc; and as to the latter point I would suggest that such relinquishment be "under such terms and conditions as the mortgagee deems necessary or appropriate to insure actual application of such proceeds to such purpose"--with the other provisions of section 10 as to application to the mortgage debt.

12. Section 11, page 16. Right to make alterations and substitutions. It might be as well to add to this provision something to the effect that any such additions, etc. shall be subject to the mortgage as expressly provided earlier therein.

13. Section 12, page 17. Condemnation.

This provides for assignment of the entire condemnation award to the mortgagor. In some circumstances part of the award might be for the purpose of covering expense of repairing or reconstructing an affected improvement--and in that case the mortgagor would probably want the benefit of that part of the award in like manner as in case of insurance; although, of course, if the mortgagor does not raise the point it is immaterial. In this connection see item 6 in the enclosed form of trust deed.

14. Section 18, page 26.

Note what was said earlier about reinstatement following default, under CC 2924c.

15. Section 19, page 27. Assignment of rents.

This provides that in the "event of default the mortgagor will

assign * * * unto the mortgagee all the rents * * * thereafter becoming due under * * * any lease * * * or any agreement for the use * * * of the mortgaged property". I would prefer an immediately effective assignment of all rents and profits coupled with a provision authorizing the mortgagor to collect pending default. Such provisions are contained in the enclosed form of trust deed--the basic provision following the description of the encumbered property reading:

> "Together with the rent, issues and profits thereof, subject, however, to the right, power and authority hereinafter given to and conferred upon beneficiary (mortgagee) to collect and apply such rents, issues and profits."

The supplementary provision is contained in section 10 of that form.

16. First Section 20, page 28.

This section apparently contemplates that the mortgagee shall have an independent power of sale (as well as the statutory right to foreclose by action). Since 1917 mortgagee powers of sale as to mortgaged real property have been valid under CC 2924--but you will note the qualifications in that section as to the manner of sale.

You might consider the expediency of fortifying the express power of sale by language to the effect that the power thereby granted is to the full extent permitted by law including without limitation section 2924.

As I have said, as to personal property the chattel mortgage may be foreclosed either by action or in the manner of a pledge sale. CC 3002 requires notice of sale to the pledgor but section 3003 provides that such notice as well as demand may be waived and the decisions support that. First National v. Landreth, 16 P2d 1010. Such waiver might be advisable.

The provision is that the property may be sold "as a whole

or in parts or parcels * * *", etc. I would prefer a provision along the lines of that in the enclosed trust deed form to the effect that the property may be sold "either as a whole or in separate parcels and in such order as it may determine" with the express right to postpone sale by announcement, etc., and with further provisions as to the effect of the conveyance on the sale such as in section 11 of the trust deed form. I would also like an express provision that the mortgagee itself may be the purchaser at the sale whether or not conducted by it. It has been said that a chattel mortgagee cannot purchase at a sale conducted by him or his agent--at least in the absence of an agreement to such effect (10 Cal. Jur. 2d 402; Henderson v. Fisher, 176 P. 63); and the rule would appear equally applicable to real estate. And it might be well in this connection to emphasize that the power of sale and the right of foreclosure by action are separate remedies, either of which may be exercised--although there is, of course, a general provision to that effect in section 22 of the form.

17. Second Section 20, page 29.

This contemplates that in case of a foreclosure action a receiver may be appointed to collect rents during pendency of the action and also "in case of sale and a deficiency during the statutory period of redemption", etc. but following foreclosure sale under court decree the purchaser at the sale is entitled by statute to collect the rents and profits until there is a redemption--subject to the qualification that in case of redemption such collections are to be credited on the redemption money (CCP 707) so that a receiver is not necessary for that period--and the provision for such appointment in case there is a "deficiency" would probably be inapplicable in view of the fact that there can be no deficiency judgment as to the real estate mortgage.

18. Section 23, page 32. Waiver, etc.

I notice this particular form refers to the laws of Texas and that, of course, will be changed here. It constitutes a waiver of various exemptions, etc. Perhaps it might be well for what it is worth to add a waiver of all notices and demands otherwise required for enforcement of any right or remedy of the mortgagee.

THE DEED

19. This is in form and effect a quitclaim--(as contemplated by section 7 of the sale instructions, which also provide that the purchaser shall procure its own evidence of title).

Since apparently such basis of sale must be accepted by the purchaser, any comment here with respect thereto is probably superfluous. However, in passing I may say that, while from the purchaser's viewpoint that should occasion no practical difficulty as to the real property since the purchaser will obtain title insurance with respect thereto, the situation is somewhat different as to the personal property covered by the deed (machinery, tools, furniture, etc., as distinguished from the raw materials, etc. to be covered by the bill of sale), since title insurance will not be obtainable as to such personal property--other than by way of chattel mortgage search, which is only assurance against specific recorded liens without positive assurance of title.

I note that the deed refers to the parties as "Grantor" and "Grantee"--and while that does not affect its nature as a quitclaim (in view of the expressed provisions against warranty) I would prefer, merely as a matter of form, to use other terms as for instance,

"Transferor" and "Transferee"--because of the fact that the terms grantor and grantee are customarily used with respect to a "grant" and by our statute (CC 1113) "from the use of the word 'grant' in any conveyance * * * unless restrained by express terms" covenants are implied (1) that the grantor has not previously conveyed the same estate or any right, title or interest therein to anyone else, and (2) that the estate is then free "from encumbrances done, made or suffered by the grantor or any person claiming under him"--which includes with other things taxes and other liens. In view of the restraining words in the deed the foregoing is obviously merely as to a minor matter of form.

Further in that connection, in view of the statutory provision as to implied "covenants" I would prefer to modify the restraining words in the deed to read something like "without any representation, assurance, convenant or warranty whatsoever, either express or implied".

For similar reasons and again merely as to form following "Group F" on page 2 I would prefer to change the words "property is conveyed" to "property which is so transferred" or "so conveyed"--so as to tie in with the earlier quitclaim limitation.

Since the transfer is merely a quitclaim it is, of course, unnecessary to list the existing matters as to which it is subject (as distinguished from new ones such as the right reserved to the United States and the Atomic Energy Commission)--although it is obviously better practice to do so as is done on page 2. In that connection it occurs to me that so long as certain of such existing matters have been covered you may want to include others such

for instance as:

- taxes, assessments and other liens and charges
- encroachments on or by the property
- covenants, conditions, restrictions, reservations, etc. (without limitation to those for highway purposes).

20. At the bottom of page 3 it is recited that "as consideration for this conveyance the grantee has paid * * * in the following manner:

(a) $ _____ in cash; and

(b) $ _____ in the form of a Promissory Note".

As suggested with respect to the mortgage, this indicates that the mortgagor's obligation has been accepted as payment. Assuming the validity of the mortgage lien, etc. that is probably immaterial as a practical matter. However, the general rule appears to be that nothing is payment except payment itself unless the parties otherwise agree--and that has been applied with respect to promissory notes.

See: 40 Am. Jur. page 775
70 CJS page 229
40 Cal. Jur. page 920
Hammond Lumber v. Richardson, 285 P. 851

While there may be no practical disadvantage in accepting the mortgage note as payment, if that is not necessary there appears to be no advantage in it and conceivably it could be disadvantageous.

INSTALLMENT NOTE

21. I have no comment as to this other than to say that while the provision for acceleration of maturity for default is proper and should be included, it is necessarily subject to the statutory reinstatement provisions hereinbefore mentioned, assuming the government is bound by local law.

BILL OF SALE

22. I do not think of anything peculiar to California as to this. The Uniform Sales Act is in effect in California including its provisions as to warranty (CC 1733). It is understood that title to the items to be covered by the bill of sale will pass immediately with no security lien reservation. I see no need for recordation of the bill of sale--although perhaps the purchaser might want it. It seems to me therefore that any standard form indicating transfer and the property affected and the limitation as to warranty, etc. should suffice--although, of course, we may anticipate the possibility that as with respect to the other instruments the purchaser may ask some modification of form.

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If this letter appears unduly lengthy, as is perhaps the fact, it has been with no thought of criticism or hypertechnicality, since, as stated, the instruments are well prepared and my only thought has been that if I were to be at all helpful that could best be done by outlining whatever occurred to me in review, and, as stated, many of the points mentioned are obviously minor.

Yours truly,

Harry A. Keithly

800623

Enclosure
HAK:cs
cc-Harold W. Sheehan, Esq.
General Counsel, Rubber Producing Facilities Disposal Commission